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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1928.

No. ~~807~~ 61

E. FRANKLIN BREWSTER, PETITIONER,

v.

BERT P. GAGE, COLLECTOR OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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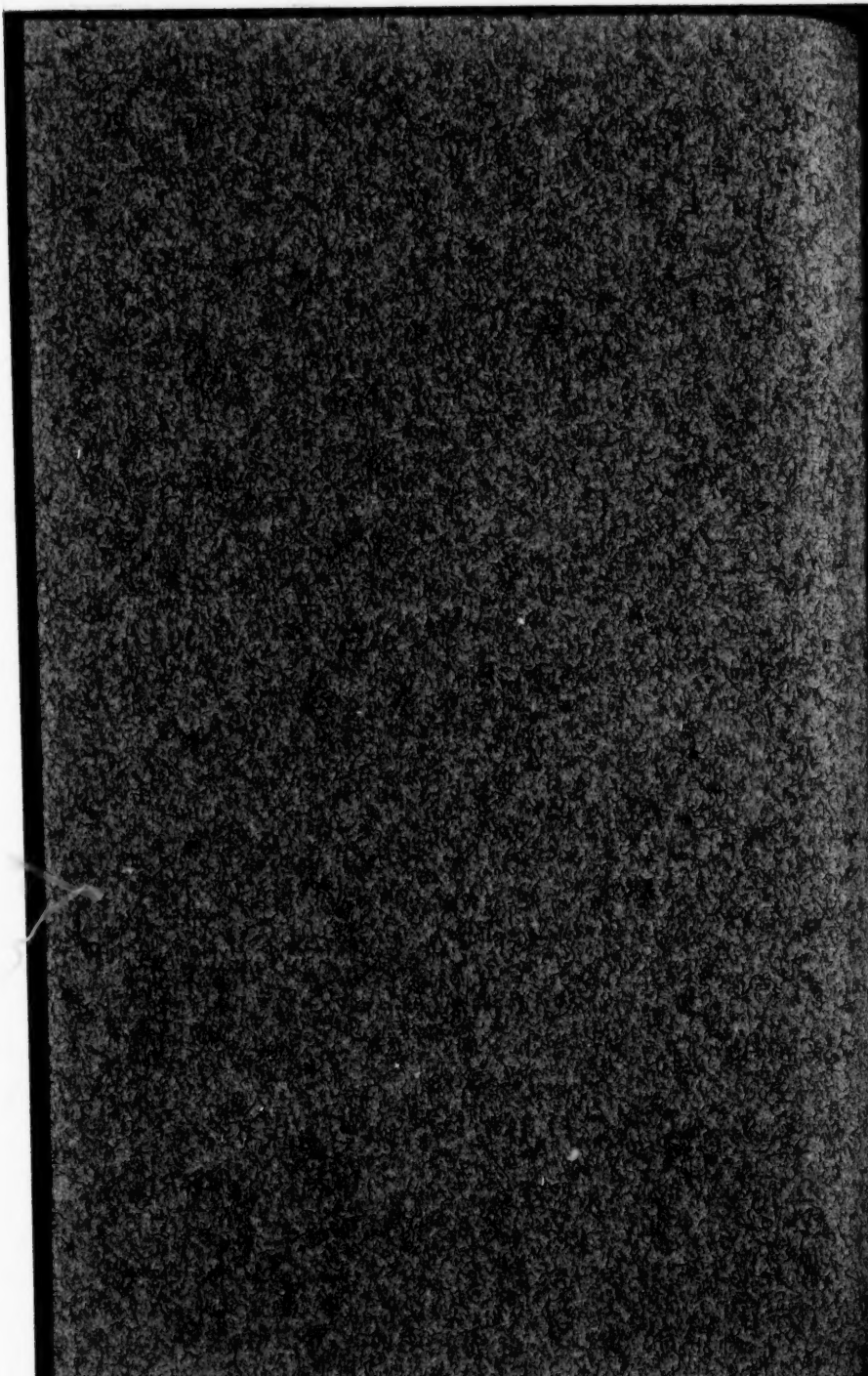
(34,116)



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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1928.

No. 807

E. FRANKLIN BREWSTER, PLAINTIFF-PETITIONER,

v.

BERT P. GAGE, COLLECTOR OF INTERNAL REVENUE, DEFENDANT-RESPONDENT.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

To the Honorable the Justices of the Supreme Court of the United States:

The petition of E. Franklin Brewster respectfully shows as follows:

First. This is a petition for a writ of certiorari to review a final determination of the Circuit Court of Appeals for the Second Circuit made and entered in

said court on the 11th day of February, 1929, reversing a judgment of the United States District Court for the Western District of New York entered January 16, 1928, in favor of the plaintiff for $2711.12.

Second. This action was brought to recover additional income taxes for the calendar years 1920, 1921 and 1922, which plaintiff claimed had been erroneously and illegally assessed and collected for the following reason: These additional income taxes were caused by the action of the Commissioner of Internal Revenue in determining as taxable profits the difference between the value of certain securities as of the date of the death of plaintiff's father and the price realized by the plaintiff on the sale of such securities after they were distributed to him as one of the residuary legatees of his father's will. Thus, the sole question involved in the case was whether, in determining the gain on the sales of securities by one of five residuary legatees the cost of such securities should be taken at their value as of the date of the decedent's death or at their value on the date of the Surrogate's order for their distribution. This question involves a construction of Section 202 (*a*) of the Revenue Act of 1921, which provides:

> "(3) In case of such property, acquired by bequest, devise or inheritance, the basis shall be the fair price or value of such property at the time of such *acquisition.*"

The District Court held that the cost of the securities should be taken at the value on the date of the Surro-

gate's order of distribution, in accordance with the decisions of the appeal of *F. W. Matthiessen, Jr.*, 2 B. T. A. 921; *Alice Fisher Foster v. Commissioner*, 7 B. T. A. 1137; *Nellie B. McGee v. Commissioner*, 13 B. T. A. 1181, and *F. W. Matthiessen, Jr., v. United States*, decided by the Court of Claims on November 7, 1927 (Commerce Clearing House Federal Tax Service for 1927, vol. 3, page 7535; Certiorari denied 73 L. ed. 21). The United States Circuit Court of Appeals for the Second Circuit reversed the decision of the District Court, so that the Federal courts are now in conflict, the Board of Tax Appeals and the Court of Claims holding in accordance with the plaintiff's claim and the United States Circuit Court of Appeals for the Second Circuit holding to the contrary.

Third. There are the following special and important reasons why a writ of certiorari should be granted:

(*a*) The decision of the Circuit Court of Appeals is in conflict with the decisions of the Board of Tax Appeals and the Court of Claims.

(*b*) The Circuit Court of Appeals has decided a Federal question in a way probably in conflict with applicable decisions of this court (U. S. *v.* Jones, 236 U. S. 106).

(*c*) The Circuit Court of Appeals has decided a question of general importance and a question of substance relating to the construction of a statute of the United States, which has not been, but should be, set-

tled by this Court. Counsel for the defendant in their brief before the Circuit Court of Appeals stated that there have been "undoubtedly several hundred thousand of settlements of tax liabilities" involving the construction here in question. Upon information and belief there are now pending numerous cases in the Board of Tax Appeals involving millions of dollars of taxes depending on this identical question. Petitioner's counsel are in receipt of a letter from a firm of attorneys in Detroit, Michigan, stating that they have five cases pending before the Board of Tax Appeals for three clients where about $9,000,000 in additional taxes depends on the question involved in this case.

WHEREFORE your petitioner prays that this Honorable Court will grant its writ of certiorari directed to said Circuit Court of Appeals for the Second Circuit, requiring the complete record of this cause in said court to be certified to this Court, and that this Court will thereupon proceed to correct the errors herein complained of.

And your petitioner will ever pray.

E. FRANKLIN BREWSTER,
Petitioner.

GURDON W. FITCH,
CASTLE & FITCH,
Counsel for Petitioner.

STATE OF NEW YORK,
Western District of New York, ss:

E. Franklin Brewster, being duly sworn, deposes and says that he is the petitioner above named; that the foregoing petition is true to his own knowledge except as to the matters therein stated to be alleged upon information and belief and as to those matters he believes it to be true.

E. FRANKLIN BREWSTER.

Sworn to before me this 22nd day of March, 1929.

[SEAL.] VILAS M. SWAN,
Notary Public.

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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1928.

No. 807

E. FRANKLIN BREWSTER, PLAINTIFF-PETITIONER,

v.

BERT P. GAGE, COLLECTOR OF INTERNAL REVENUE, DEFENDANT-RESPONDENT.

BRIEF ON BEHALF OF PETITIONER.

This is a petition for writ of certiorari to be directed to the Circuit Court of Appeals for the Second Circuit. The action was brought by the petitioner to recover additional income taxes claimed to have been illegally collected by the defendant. The plaintiff recovered judgment in the United States District Court for the Western District of New York for $2,711.12 (R. 30-31). The opinion of the District Judge is reported in 25 Fed. Rep., 2nd series, at page 915. This judgment was reversed by the Circuit Court of Appeals for the Second Circuit by order entered February 11, 1929

(R. 50). The opinion of the Circuit Court of Appeals appears at page 45 of the record. The sole question involved in the appeal was whether in determining the gain on sales of securities by a residuary legatee the cost of said securities should be taken at their value as of the date of the testator's death or at their value on the date of the Surrogate's order for distribution.

Section 202 (*a*) of the Revenue Act of 1921 provides:

> "(3) In the case of such property, acquired by bequest, devise, or inheritance, the basis shall be the far price or value of such property at the time of such *acquisition.*"

Section 213 of the Act of 1918 provides that the term "gross income" does not include

> "(3) The value of property *acquired* by gift, bequest, devise or descent (but the income from such property shall be included in gross income); * * *"

The question involved on this appeal, therefore, depends upon the definition of the word "acquire."

Prior to the decision by the Circuit Court of Appeals the Federal Courts had already four times passed upon this question and in every instance in accordance with the plaintiff's contention.

Appeal of F. W. Matthieson, Jr., 2 Bt. T. A. 921.

Alice Fisher Foster v. Commissioner, 7 B. T. A. 1137.

Matthieson v. U. S. decided by the Court of Claims on November 7, 1927. The opinion of

the Court of Claims has not yet been officially reported, but is set forth in the Commerce Clearing House Federal Tax Service for 1927, vol. III, page 7535 (certiorari denied 73 L. ed. 21).

Nellie B. McGee v. Commissioner, 13 B. T. A. 1181.

Furthermore, the Revenue Act of 1928 has adopted plaintiff's contention as the proper rule. Section 113 contains the following provisions:

> "(5) Property Transmitted at Death.—* * * If the property was acquired by the decedent's estate from the decedent, the basis in the hands of the estate shall be the fair market value of the property at the time of the death of the decedent. In all other cases if the property was acquired either by will or intestacy, the basis shall be the fair market value of the property at the time of the distributions to the taxpayer."

Point I.

Upon a testator's death, title to personal property not specifically bequeathed, together with the rights to possess, manage and sell, pass to the executor or administrator and not to the legatees.

This old common-law rule has never been changed by statute. The executor or administrator has exclusive legal title to personal property not specifically bequeathed, has the right to possession even as against

legatees, and has the right to sell and transfer a good title free and clear from all claims of creditors or legatees.

One of the leading text writers states the rule as follows (*Schouler on Wills,* sec. 2061):

> "The legal and equitable title to all personal property of the deceased, including choses in action and in corporeal rights, vests in fact in the executor or administrator, as against all the others, during the suitable period for administration, and he holds this property as a trustee and proper representative of all the parties interested herein, wherever such property may be situated, and whether such personalty is in the possession of the deceased at death or is recovered by the representative thereafter."

The New York rule was thus stated by the Court of Appeals in *Peterson v. Chemical Bank,* 32 N. Y. 21:

> "The devolution of ownership is direct to the representative *and the beneficiaries take no title in the specific property which the law can recognize.*"

In *Matter of Zefita,* 167 N. Y. 280, at page 283, the York Court of Appeals quoted with approval from an earlier decision as follows:

> "He had the right to claim the amount of money which his share the residuary estate of Mrs. Fogg would result in, nothing more; no particular piece of property, no particular sum of money, no particular represefitatives of money or property. And until this residuary

> estate was ascertained by an accounting of the executors, the legatee might not be even able to maintain an action for its recovery."

In a recent decision in *State v. Circuit Court of La Crosse County,* 177 Wis. 548, at page 554, the court said:

> "The administrator is the legal owner, for the time being, of the personal property of which the decedent died possessed, and his title and authority extend so completely to all such property as to exclude, for the time being, creditors, legatees and all other beneficiaries interested in the estate."

In *Norton v. Lilley,* 210 Mass. 214, the Supreme Court of Massachusetts said:

> "If an attorney employed by an administrator to help him in the winding up of an estate robs the estate or neglects his duty to it, the administrator in whom is the title to the personal property constituting the estate and with whom the contract in such a case is made by the attorney, is the person who has the right to bring an action for the wrong so done. Such an action cannot be brought by a distributee because he has no title to the personal property. * * * The distributee's right is a right to have the estate properly wound up and distributed."

This Court had occasion to state the rule in the case of *United States v. Jones,* 236 U. S. 106, in which the Court said, at page 112:

> "It hardly needs statement that personal property does not pass directly from a decedent to

> legatees or distributees, but goes primarily to the executor or administrator, who is to apply it, so far as may be necessary, in paying debts of the deceased and expenses of administration, and is then to pass the residue, if any, to legatees or distributees. If the estate proves insolvent, nothing is to pass to them. So, in a practical sense their interests are contingent and uncertain till, in due course of administration, it is ascertained that a surplus remains after the debts and expenses are paid. Until that is done, it properly can not be said that legatees or distributees are certainly entitled to receive or enjoy any part of the property. The only right which can be said to vest in them at the time of the death is a right to demand and receive at some time in the future whatever may remain after paying the debts and expenses."

To be sure, an executor is trustee of personal property for the benefit of creditors and legatees, but in the same manner directors are said to be trustees for stockholders. Yet, when the corporation sells property at more than its cost the stockholders make no gain as individuals.

Point II.

The securities in question were not "acquired" by the plaintiff under the terms of the statute or for income-tax purposes until the surrogate's order of distribution.

The word "acquire" is defined by Bouvier's Law Dictionary as follows:

> "To make property one's own; to gain permanently. It is regularly applied to a permanent acquisition. A man is said to obtain or procure a mere temporary acquisition. * * *"

There can, of course, be no doubt that a residuary legatee has an immediate interest in testator's estate which he can assign and which will pass under his will or under the laws of intestacy. Furthermore, there is no question but that this interest becomes vested for such purposes on the date of the testator's death. In such a case if a legatee sold such an undivided interest, he would undoubtedly make a profit measured by the difference between the sale price and the value of such undivided interest at the date of testator's death.

On the other hand, as pointed out under Point I, a legatee, except in case of specific legacies, has no legal title to any security or particular item of personal property. Not only has he no legal title, but he has no right of possession or of sale. How then, can he be said to have "acquired" the securities in question?

This distinction between an undivided interest in an estate and the title to specific securities of the estate is clearly pointed out by the Board of Tax Appeals and the Court of Claims in the Matthiessen case. The Board of Tax Appeals in the Matthiessen appeal said, at pages 928 to 929:

> "It is true the taxpayer did acquire a right on the death of the testator, but that right was not a property right in the stock which was the subject matter of the transaction involved in this appeal. The most that the taxpayer,

as residuary legatee, could demand at the time of the death of the testator was a proper administration of the estate and a distribution of such assets as remained after all debts and claims were settled. *Irwin v. Sample*, 72 N. E. 687; *Norton v. Lilley*, 96 N. E. 351; United *States v. Jones, supra; Anderson v. Shepard*, 121 N. E. 215; *In re Waban Rose Conservatories*, 106 N. E. 137.

"From the authorities cited it appears that, although the taxpayer had a right to the proper administration of the estate and to a proportionate share of the residue remaining, he had no right or title in the stock in question until distribution was made by the executors. The date on which he acquired the property in the stock was the date of its distribution, and any amount representing an increase in the value of the stock between the date of the death of the testator and the date of such distribution should not be included in the income of the taxpayer."

The Court of Claims in *Matthiessen v. U. S.* said the same thing in a little different language, as follows:

"Manifestly it requires no more than a mere statement that a residuary legatee under a will acquires an interest in a residuary estate on the date of the death of the testator. It is likewise obvious that he may sell and dispose of the same if he chooses. Whether the legacy is ever received in kind is, of course, dependent upon prior bequests and priority claims against the estate fixed by law. Seemingly it is elementary that until the legatee receives his legacy in possession, vested with absolute control and domin-

> ion over it, capable of asserting ownership against all the world, the contingent interest vesting at the date of the death of the testator is not merged in fee simple title."

Almost the identical question involved on this appeal was decided by the Supreme Court of Vermont in *White v. Waite,* 47 Vermont Reports, 507, where a wife's father died prior to her marriage, but his estate was not distributed until after her marriage. The question arose as to whether the personal property received by her under that distribution was "acquired" during coverture and therefore came within the provisions of the statute relating to property of married women. The Enabling Act of 1867 provided that "all personal property and rights of personal action *acquired* by any married woman during coverture, by inheritance or distribution, shall be held by her to her sole and separate use." In holding that the specific property so received by her was "acquired" at the time of distribution and not at the death of her father the court said:

> "While the right to a distributive share in her father's estate became vested in the daughter immediately upon her father's decease, and she became possessed of an undivided portion of the property of the estate, subject to the rights of the administrator to use a part of the same for the payment of the debts and expenses of administration, yet, the particular property did not become absolutely vested in her, until the decree of the probate court making distribution of the estate, became absolute. Until distribu-

> tion, she had no right as against the administrator, or other heirs, if such there were, to the specific personal property which she afterwards received from the estate. When the decree distributing the estate became absolute, she, in the language of the act, 'acquired' the specific articles of personal property decreed to her, and the right to a personal action for the recovery of the sum of money ordered to be paid to her."

A similar question arose in the case of *Alexander v. Alexander,* 85 Virginia Reports, 353, where the court had to construe the Married Woman's Enabling Act relating to "all property *acquired* by her before and during marriage." In this case the wife by the terms of her father's will was given a vested remainder in real estate after a life use, which was devised to her mother. Her father died before her marriage but as her mother did not die until after her marriage, she did not go into possession of the property until after her marriage. The court held that the property was not acquired until she received possession, citing *White v. Waite, supra.*

Counsel for defendant in his brief in the Circuit Court referred to a line of cases which merely relate to the undivided interest in the estate, which, of course, unquestionably vests at the time of the death of the testator and may be assigned by the legatee and in case of his death passes under his will. None of these cases, however, relate to the vesting of the legatee's interest in any particular security.

Point III.

Executors and administrators are considered as owners of personal property for purposes of taxation.

It has been uniformly held by the various states that personal property of an estate for purposes of direct taxation must be assessed to the executor or administrator.

Eliot v. Prime, 98 Me. 48.
Herrick v. City of Big Rapids, 53 Mich. 554.
Vaughn v. City Commissioners, 154 Mass. 143.
Brown v. Noble, 42 Ohio State 405.
Baldwin v. Shine, 84 Ky. 512.

Congress itself has recognized the executor's title to personal property by providing that during administration the income thereon shall be reported and the tax thereon paid by the executor or administrator. Sec. 219 of the Revenue Act of 1918 provides:

> "(*a*) That the tax imposed by sections 210 and 211 shall apply to the income of estates or of any kind of property held in trust, including
> (1) Income received by estates of deceased persons during the period of administration or settlement of the estate."

As pointed out by the Board of Tax Appeals in the Matthiessen case:

> "From these provisions it appears that Congress recognized that the property of a decedent vested in the executor or personal representative during the period of administration and

> provided, in order that such estates might not escape taxation, that any gain derived during such period should be paid by such executor or personal representative."

How can securities of an estate in process of administration be said to belong to the legatees if the income thereon is taxable to the executor and if profits on sales thereof by the executor are taxable against the estate?

Point IV.

The construction adopted by the District Court leads to no more difficulties or inconsistencies than that contended for by the plaintiff.

Defendant raises the objection that under the rule adopted by the District Court the Government will receive no income tax on the increase in value between the time of testator's death and the date of distribution. The same is true as to the increase in value between the time securities are purchased and the value at the time of testator's death. While the Treasury Regulations provided that this appreciation was taxable, the courts held that it was not. Likewise, prior to December 31, 1920, there was no tax on the increase in value of securities between the time they were purchased by a donor and the date of their gift to the donee. However, the fact that there may be income upon which the Government receives no tax is no reason for putting a strained construction on the statute. As said by Chief Justice Taft in *Smietanka v.*

First Trust & Savings Bank, 257 U. S. 602, at page 606:

> "It may be that Congress had a general intention to tax all incomes, whether for the benefit of persons living or unborn, but a general intention of this kind must be carried into language which can be reasonably construed to effect it. Otherwise the intention cannot be enforced by the courts. The provisions of such acts are not to be extended by implication."

Difficulties surrounding an adoption of the defendant's contention will lead to much greater inconsistencies than those pointed out by him. Suppose, for example, on distribution a legatee accepts in lieu of cash securities then worth $50,000 but which were appraised at only $10,000 on the date of testator's death. If the legatee later sold these securities for $50,000, under the defendant's theory he would be making a profit of $40,000 and this in the face of the statute, Sec. 213 of the Revenue Act above quoted providing that legacies are exempt from income tax. On the other hand, suppose that the securities so received on distribution at a valuation of $50,000 were worth $150,000 at the time of testator's death. On defendant's theory the legatee would thereby suffer a deductible loss of $100,000.

Again suppose that one of the residuary legatees purchases securities from the executor. Under the defendant's theory what would be the cost of these securities?

Obviously none of the objections raised by defendants or in the opinion of the Circuit Court of Appeals seemed serious to Congress since in the Revenue Act of 1928 it adopted the rule contended for by the plaintiff (Sec. 113 above quoted).

POINT V.

Congress is not bound by constructions placed by the Treasury Department on the revenue acts of former years.

The opinion of the Circuit Court of Appeals points out that the Treasury Department in construing the acts since 1913 has consistently ruled in accordance with defendant's contention. There is no evidence of these rulings in the record, though the Court probably can take judicial notice thereof. While "great weight" might properly be given to "long continued" construction of statutes by department officials, it should be borne in mind that Treasury rules in the last few years have changed so rapidly that it is almost impossible to keep up with them. In any event, as pointed out by this Court in *U. S. v. Finnell,* 185 U. S. 236, "If the departmental construction of the statute in question were obviously or clearly wrong, it would be the duty of the court to so adjudge."

Many times after Congress has re-enacted the income tax provisions of former acts which have been construed by the Treasury decisions, the Commissioner has not hesitated to revise his rulings, even making them retroactive. To give only one of many examples,

Regulations 33, Article 8, related to the purchase of mortgaged property by a mortgagee upon foreclosure sale. After these regulations were in force the Acts of 1918 and 1921 were passed re-enacting the provisions of the Act of 1913. Yet on December 21, 1921, by T. D. 3264, the Commissioner purported to amend those regulations 33 making them retroactive to 1913.

Conclusion.

A WRIT OF CERTIORARI SHOULD BE GRANTED.

Respectfully submitted,

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